UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF INDIANA
SOUTH BEND DIVISION

IN THE MATTER OF	)	
	)	
THOMAS J. STEWART, SR., and	)	CASE NO. 04-31187 HCD
JANELL A. STEWART,	)	CHAPTER 7
	)	
DEBTORS.	)	
	)	
	)	
CARMELO ROSARIO and	)	
MIRIAM ROSARIO,	)	
PLAINTIFFS,	)	
vs.	)	PROC. NO. 04-3077
	)	
THOMAS J. STEWART, SR., and	)	
JANELL A. STEWART,	)	
DEFENDANTS.	)	

Appearances:

Fred R. Hains, Esq., attorney for plaintiffs, 125 North St. Peter Street, South Bend, Indiana 46617;

Mario J. Zappia, attorney for defendants, 52582 State Road 933 North, South Bend, Indiana 46637; and

Jacqueline Sells Homann, Trustee, Jones Obenchain LLP, P.O. Box 4577, South Bend, Indiana 46634.

MEMORANDUM OF DECISION

At South Bend, Indiana, on January 19, 2005.

Before the court are the Motion for Summary Judgment, filed by the plaintiffs Carmelo Rosario and Miriam Rosario ("plaintiffs") on September 13, 2004, and Defendant's [*sic*] Response to Plaintiff's [*sic*] Motion for Summary Judgment, filed by the defendants Thomas J. Stewart, Sr., and Janell A. Stewart ("defendants") on October 13, 2004. Summary judgment is sought on the plaintiffs' Complaint to Determine Dischargeability of Debt under 11 U.S.C. § 523, filed on June 14, 2004. The complaint asks the bankruptcy court to find that the state court default judgment awarded to the plaintiffs is a nondischargeable debt incurred by the debtors pursuant to 11 U.S.C. § 523(a)(2)(A) or § 523(a)(6). For the reasons that follow, the court denies the plaintiffs' Motion for Summary Judgment.

Jurisdiction

Pursuant to 28 U.S.C. § 157(a) and Northern District of Indiana Local Rule 200.1, the United States District Court for the Northern District of Indiana has referred this case to this court for hearing and determination. After reviewing the record, the court determines that the matter before it is a core proceeding within the meaning of § 157(b)(2)(I) over which the court has jurisdiction pursuant to 28 U.S.C. §§ 157(b)(1) and 1334. This entry shall serve as findings of fact and conclusions of law as required by Federal Rule of Civil Procedure 52, made applicable in this proceeding by Federal Rules of Bankruptcy Procedure 7052 and 9014. Any conclusion of law more properly classified as a factual finding shall be deemed a fact, and any finding of fact more properly classified as a legal conclusion shall be deemed a conclusion of law.

Background

The plaintiffs purchased a house in Mishawaka, Indiana from the defendants on September 21, 2000. The defendants had signed a disclosure form stating that the septic and plumbing systems of the property were not defective, and the plaintiffs relied on that statement when they decided to buy the home. However, in their state court complaint, filed in the St. Joseph Circuit Court, Mishawaka Division, on August 8, 2002, the plaintiffs alleged that both systems were defective when they purchased the property and that the defendants were aware of the problems when they signed the disclosure form. *See* R.1, Ex. B at 1. They further alleged that they could not have discovered the problems by inspection before taking possession. The plaintiffs claimed damages plus attorney fees and costs. When the defendants did not respond to the complaint, the plaintiffs filed a motion for default judgment. On December 18, 2002, the St. Joseph Circuit Court granted the plaintiffs a default judgment in the amount of $11,270 in damages and $3,332 in attorney fees.

On March 10, 2004, the defendants filed a voluntary chapter 7 bankruptcy petition. Three months later, the plaintiffs filed this adversary proceeding in the bankruptcy court. The complaint initiating that proceeding raised the same factual allegations that the plaintiffs had presented in the state court complaint and

sought a determination in this court that the default judgment award was nondischargeable in bankruptcy. They claimed that the debt was incurred as a result of the debtors' false representations and willful and malicious injury to the plaintiffs, and therefore was excepted from discharge pursuant to §§ 523(a)(2)(A) and (a)(6). The defendants filed their answer to the complaint, admitting the state court default judgment but denying the underlying facts.

On September 13, 2004, the plaintiffs filed a motion for summary judgment on the complaint. According to the plaintiffs, the recent decision of the Seventh Circuit Court of Appeals, *In re Catt*, 368 F.3d 789 (7th Cir. 2004), was directly on point in this case. The plaintiffs stated that *In re Catt* held that default judgments in Indiana were entitled to preclusive or collateral estoppel effect in bankruptcy proceedings. In the same way, insisted the plaintiffs, the default judgment against these defendants is binding on this court and summary judgment should be granted.

A month later, the defendants opposed the motion and noted factual distinctions between *In re Catt* and the present case. They argued that they were not given the opportunity to have a full and fair hearing on the state court complaint because they never had actual knowledge of the complaint. Moreover, they noted certain material issues of fact in the case. They asked that the court deny the plaintiffs' motion for summary judgment.

The court took the matter under advisement on November 3, 2004.

Discussion

A court renders summary judgment when the "pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law." Fed. R. Civ. P. 56(c); Fed. R. Bankr. P. 7056; *see Celotex Corp. v. Catrett,* 477 U.S. 317, 322, 106 S. Ct. 2548, 2552, 91 L.Ed.2d 265 (1986); *Tegtmeier v. Midwest Operating Engineers Pension Trust Fund,* 390 F.3d 1040, 1045 (7th Cir. 2004). The moving party bears the initial burden of demonstrating that no genuine issue of material fact exists. *See Celotex*, 477 U.S. at

323. If the moving party satisfies its initial burden, then the nonmoving party must "go beyond the pleadings and by [its] own affidavits, or by the 'depositions, answers to interrogatories, and admissions on file,' designate 'specific facts showing that there is a genuine issue for trial.'" *Id.* at 324 (quoting Fed. R. Civ. P. 56(e)). The court neither weighs the evidence nor assesses the credibility of witnesses. *See Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 249, 106 S. Ct. 2505, 2511, 91 L.Ed.2d 202 (1986). Summary judgment must be granted "against a party who fails to make a showing sufficient to establish the existence of an element essential to that party's case, and on which that party will bear the burden of proof at trial." *Celotex*, 477 U.S. at 322.

The plaintiffs claim that they should be awarded summary judgment in this adversary proceeding because their Indiana state court default judgment is entitled to preclusive or collateral estoppel effect in bankruptcy proceedings. They assert that the default judgment against the defendants, in this case and in *In re Catt*, was based on fraud. Pursuant to the holding in *In re Catt*, they argue, this bankruptcy court is bound by the plaintiffs' default judgment and the defendants are precluded from litigating the issue of fraud.

The doctrine of collateral estoppel, also called issue preclusion, prevents a party from relitigating issues previously determined in another court. *See Brown v. Felsen*, 442 U.S. 127, 139 (1979); *Jensen v. Foley*, 295 F.3d 745, 748 (7th Cir. 2002). "The effect of a judgment in subsequent litigation is determined by the law of the jurisdiction that rendered the judgment . . . provided the judgment was rendered in a proceeding that comported with due process of law." *In re Catt*, 368 F.3d at 790-91 (citing 28 U.S.C. § 1738 and supporting case law). The Court of Appeals of Indiana recently set forth the factors for determining the preclusive effect of a judgment rendered by an Indiana court:

> Issue preclusion, often referred to as collateral estoppel, bars subsequent litigation of a fact or issue which was necessarily adjudicated in a former lawsuit if the same fact or issue is presented in the subsequent lawsuit. In that situation, the former adjudication will be conclusive in the subsequent action even if the two actions are on different claims. However, the former adjudication will only be conclusive as to those issues which were actually litigated and determined therein.
>
> Collateral estoppel does not extend to matters which were not expressly adjudicated and can be inferred only by argument. The primary consideration in the use of collateral estoppel is whether the party against whom the former adjudication is asserted had "a full and fair opportunity to litigate the

> issue and whether it would be otherwise unfair under the circumstances" to permit the use of issue preclusion in the subsequent action.

American Family Mut. Ins. Co. v. Ginther, 803 N.E.2d 224, 230 (Ind. Ct. App. 2004). The Seventh Circuit, in *In re Catt*, examined Indiana's "primary consideration," which was whether there had been a full and fair opportunity to litigate the issue.

This court finds that there are indeed numerous similarities between this adversary proceeding and the one examined by the Seventh Circuit in *In re Catt*. In both cases, the plaintiffs brought suit in state court, alleging fraudulent conduct on the part of the defendants. The plaintiffs won a default judgment against the defendants and were awarded damages. In both cases, the defendants then filed a chapter 7 petition and the creditors, in turn, filed a nondischargeability complaint against the debtors-defendants, alleging that the judgment was not dischargeable under § 523(a)(2)(A). In *Catt*, the appellate court reversed the bankruptcy court's determination that the state court's finding of fraud was not binding in the bankruptcy proceeding because the doctrine of collateral estoppel did not apply. According to the plaintiffs, the holding of the court of appeals in *In re Catt* was that "a default judgment is entitled to preclusive effect." R. 13, Ex. A, at 4 (quoting *In re Catt*, 368 F.3d at 792). The plaintiffs insist that, in light of the similar circumstances herein, this court must follow *Catt* and find that the default judgment for fraud against the defendants is binding on this court.

The court finds that the plaintiffs have based their claim on a partial quotation which omits a crucial qualifier in *Catt*. The appellate court held that a default judgment, or one based on proceedings "that were the functional equivalent of default proceedings," is entitled to preclusive effect "provided that the loser had a fair chance . . . for a full and fair hearing." *Id.* at 792. *In re Catt* focused on the due process requirement that the losing party must have had the opportunity for a "full and fair hearing." Because Indiana was the jurisdiction rendering the judgment at issue, the circuit court examined Indiana's treatment of default judgments. It found:

> [A] significant minority of states, Indiana among them, allow[s] findings made in default proceedings to collaterally estop, provided that the defaulted party could have appeared and defended if he had wanted to. For, in such a case the party has in effect forfeited his right to a full and fair hearing.

Id. at 791. It concluded that, in Indiana, "due process does not require in every case either a hearing or that a particular issue be 'actually litigated'; it requires that the party sought to be precluded have an opportunity for a hearing." *Id.* at 792.[1] In *In re Catt*, it found, the defendant had that opportunity: He knew about the suit and knew a trial was scheduled, but did not appear for it. In the appellate court's view, the defendant "was determined to bypass the state court litigation in the hope that any judgment rendered against him in that suit would be wiped out by a discharge in his anticipated bankruptcy." *Id.* The court of appeals concluded:

> [H]ad there been no 'trial' at all but merely the entry of a default judgment on motion by the [plaintiffs] when [the defendant] failed to appear at the trial, the state court's finding of fraud, being an essential predicate of the judgment would, under Indiana law and consistent with due process (and therefore binding on the bankruptcy court), have had the same collateral estoppel effect as if the finding had been made after a full adversary proceeding. . . . If, as we have just held, a default judgment is entitled to preclusive effect, so must a judgment based on proceedings as abbreviated as this one – proceedings that were the functional equivalent of default proceedings – provided that the loser had a fair chance, which he booted, for a full and fair hearing.

Id. The key test, according to the appellate court, therefore, is "whether by allowing himself to be defaulted or otherwise, a party has forfeited his right to such a hearing." *Id.* If he has, said the Seventh Circuit, he cannot complain. *See id.*

In light of the *In re Catt* decision, therefore, the court turns to the circumstances of the case now before it. It first considers whether the defendants, the party sought to be precluded in the adversary proceeding, had an opportunity for a full and fair hearing. In their brief, the defendants stated that notice of the lawsuit was given by publication. They never had actual notice of the pending suit filed against them, they asserted, for they were living in Georgia at the time. They claimed that they therefore were not given the opportunity for a full and fair hearing.

---

[1] *See also Small v. Centocor, Inc*., 731 N.E.2d 22, 28 (Ind. Ct. App. 2000) (finding that the defendant, who was in control of the first suit, was afforded a full opportunity to litigate the issues in the prior action, but failed to respond to discovery requests or to appear for a hearing, had failed to avail himself of the opportunity to litigate the issues, and thus the trial court properly entered summary judgment on the basis of collateral estoppel); *Forrester v. Staggs (In re Staggs)*, 178 B.R. 767, 776-78 (Bankr. N.D. Ind. 1994) (finding that the policy of judicial finality that underlies the doctrine of collateral estoppel requires that one fair opportunity to litigate an issue is enough and places the focus of the inquiry upon the opportunity to litigate, rather than upon the quality of the evidence or presentation).

It is well settled in Indiana that service of process by publication is a proper form of notice. "The Indiana Rules of Trial Procedure provide for service by publication when the person to be served cannot be served personally and cannot be found, had concealed his whereabouts, or has left the state." *Smith v. Tisdal*, 484 N.E.2d 42, 43-44 (Ind. Ct. App. 1985) (citing Ind. T. R. 4.5, 4.9(B)(3), 4.13). Indiana Trial Rule 4.13 governs summonses and service by publication. It provides:

> (A) Praecipe for Summons by Publication. In any action where notice by publication is permitted by these rules or by statute, service may be made by publication. . . . The person seeking such service, or his attorney, shall submit his request therefor upon the praecipe for summons along with supporting affidavits that diligent search has been made that the defendant cannot be found, has concealed his whereabouts, or has left the state, and shall prepare the contents of the summons to be published. The summons shall be signed by the clerk of the court or the sheriff in such manner as to indicate that it is made by his authority.

The fundamental requirement for notice in Indiana is that the best method of giving notice must be used and that it must be "reasonably calculated to inform defendant of the pending proceedings." *Mueller v. Mueller*, 287 N.E.2d 886, 889 (Ind. 1972). Because the type of notice required varies with the circumstances, the record in the case must show that service by publication was the best notice possible under those facts; then such service would be proper. *See id.* at 890. Service by publication was not considered sufficient, for example, when the plaintiff had knowledge of the defendant's address at the time the action was filed. *See, e.g., Smith v. Tisdal*, 484 N.E.2d at 44. Notice by publication was sufficient, however, when the facts showed that the party seeking relief made reasonable inquiry and diligent search to determine the whereabouts of the defendant. *See Bays v. Bays*, 489 N.E.2d 555, 560 (Ind. Ct. App. 1986).

In this case, the defendants alleged in their brief that they had left the state and were living in Georgia; they further stated that notice by publication, rather than actual notice, was given. The court notes that the defendants did not furnish the court with a record of the state court action; there is no evidence in the record, therefore, of the type of notice given. Moreover, the defendants did not file a sworn affidavit concerning their whereabouts or their nonreceipt of service of process. *See, e.g., Sill v. Sweeney (In re Sweeney)*, 276 B.R. 186, 191-92 (6th Cir. B.A.P. 2002) (setting aside summary judgment based in part on defendants' sworn affidavit

denying receipt of service of process); *Professional Laminate & Millwork, Inc. v. B & R Enters.*, 651 N.E.2d 1153, 1158 (Ind. Ct. App. 1995) (refusing to set aside default judgment on basis of insufficient affidavit). In fact, in the view of the court, if the defendants did leave the state, it appears that the only reasonable method of service of process was by means of publication. *See Mueller*, 287 N.E. at 890 (concluding that, without information as to the whereabouts of the defendants, the newspaper was the most likely method to convey notice). The court finds that the defendants, as the nonmoving party, failed in their burden of going beyond the pleadings, by affidavits or otherwise, to "set forth specific facts showing that there is a genuine issue for trial." Fed. R. Civ. P. 56(e); Fed. R. Bankr. P. 7056. The court will not deny a motion for summary judgment when the opposing party's response was merely allegations in its pleading. *See id.* It finds, therefore, that the defendants' challenge to summary judgment cannot succeed.

However, it does not follow from the defendants' unsuccessful challenge that the plaintiffs' motion for summary judgment will be granted. The state court judgment must meet the state's collateral estoppel requirements before the default judgment debt can be found nondischargeable in the defendants' bankruptcy. *See Pahlavi v. Ansari (In re Ansari)*, 113 F.3d 17, 21 (4th Cir.), *cert. denied*, 522 U.S. 914 (1997). In considering the collateral estoppel effect of the underlying Indiana default judgment on this bankruptcy proceeding, the court finds that an essential element for applying collateral estoppel is missing. As the Indiana Court of Appeals taught in *American Family Mutual Insurance Co.*, when the "same fact or issue" was presented in two lawsuits and was "actually litigated and determined" in the first suit, "the former adjudication will be conclusive in the subsequent action." *American Family Mut. Ins. Co.*, 803 N.E.2d at 230; *see also Small v. Centocor, Inc.*, 731 N.E.2d 22, 28 (Ind. Ct. App. 2000) (requiring identity of the issues as an essential element of collateral estoppel). In this case, the court finds that the issues decided in the prior adjudication are not identical to the issues in the current action.

In this proceeding, the plaintiffs' complaint alleges that the debt owed by the defendants under the default judgment is nondischargeable pursuant to 11 U.S.C. § 523(a)(2)(A) and (a)(6), which provide:

> (a) A discharge . . . does not discharge an individual debtor from any debt –
> . . .
> (2) for money, property, services, or an extension, renewal, or refinancing of credit, to the extent obtained by –
> (A) false pretenses, a false representation, or actual fraud . . .;
>
> . . . and . . .
>
> (6) for willful and malicious injury by the debtor to another entity or to the property of another entity.

The court finds that, to succeed under § 523(a)(2)(A), the plaintiffs had the burden of proving by a preponderance of the evidence that their debt was obtained by actual fraud or misrepresentation. *See McClellan v. Cantrell*, 217 F.3d 890, 893-94 (7th Cir. 2000). To succeed under § 523(a)(6), the plaintiffs were required to demonstrate that the defendants intended to cause harm or that there was a substantial certainty that harm would occur. *See Kawaauhau v. Geiger*, 523 U.S. 57, 61, 118 S. Ct. 974,977, 140 L.Ed.2d 90 (1998) (requiring a showing of "deliberate or intentional injury, not merely a deliberate or intentional act that leads to an injury").

However, there is no underlying finding of fraud or of willful and malicious injury in the state court default judgment. The Order of Default Judgment Against Defendant, issued by the the St. Joseph Circuit Court, Mishawaka Division, states in its entirety:

> The Court, having reviewed Plaintiff's Motion for Default Judgment and Affidavit in support of said Motion, grants the Plaintiff a default judgment and decrees that the Plaintiffs, Carmelo and Miriam Rosario, are awarded a judgment in the amount of Eleven Thousand Two Hundred Seventy Dollars ($11,270.00) representing the amount of damages suffered due to the Defendant's nondisclosure of the defects upon the sale of the property . . . plus attorney's fees in the amount of Three Thousand Three Hundred Thirty Two Dollars ($3,332.00); and all other relief in the premises.

R. 1, Ex. A. In *In re Catt*, the state court's finding of fraud was "an essential predicate of the judgment." *In re Catt*, 368 F.3d at 792. In this case, however, the state court order found "nondisclosure of the defects" but did not make a determination of fraud or an intent to cause injury. Without such findings to indicate that the state court actually decided those issues, this court determines that there is no identity of issues and no finding by the state court that binds this bankruptcy court in its determination of dischargeability of the debt owed to the plaintiffs. Even though the default judgment is valid, and even though the defendants admitted their indebtedness

to the plaintiffs under that default judgment, the judgment cannot be given collateral estoppel effect with respect to the dischargeability issues raised by the plaintiffs in their bankruptcy complaint. The court concludes that summary judgment is not appropriate in these circumstances. It therefore denies the plaintiffs' motion for summary judgment.

Conclusion

For the reasons set forth in this Memorandum of Decision, the court denies the Motion for Summary Judgment filed by the plaintiffs Carmelo Rosario and Miriam Rosario against the defendants Thomas J. Stewart, Sr., and Janell A. Stewart. A pretrial conference on the complaint will be scheduled by separate order.

SO ORDERED.

/s/ Harry C. Dees, Jr.
HARRY C. DEES, JR., CHIEF JUDGE
UNITED STATES BANKRUPTCY COURT